Written by
Oleh Kombaiev
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Symbol	Price	% Chg
AAPL	128.10	0.20%
ABNB	162.33	-3.89%
BCPC	132.63	-0.73%
BKNG	2,337.92	-1.89%
BRK.A	424,840.00	0.81%
CMG	1,426.50	-1.62%
CNSWF	1,486.72	0.05%
CTAS	348.59	-0.62%
DPZ	431.89	-0.48%
EBAY	58.24	0.95%

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Long Ideas Tech

Amazon: The Most Clearly Undervalued Company

May 06, 2021 12:03 AM ET | **Amazon.com, Inc. (AMZN)** | 9 Comments | 8 Likes

Summary

- Amazon is one of the companies whose growth has not yet reached its limit and not even entered the plateau phase.
- In terms of comparative valuation, AMZN is undervalued against the market.
- DCF-based Amazon stock price target suggests 30% upside potential. But I think this is not even a basic scenario, but a pessimistic scenario.

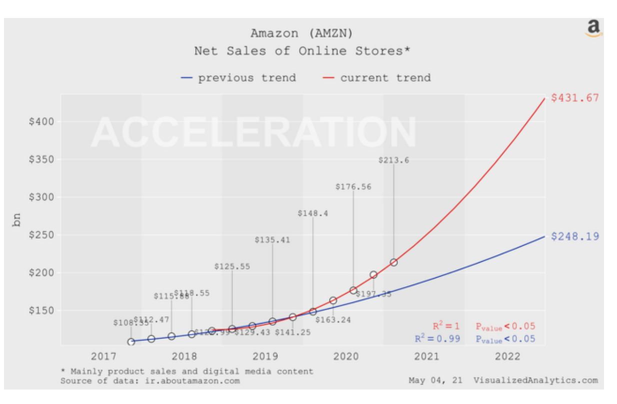
Photo by Elijah Nouvelage/Getty Images News via Getty Images

I present my comprehensive Amazon (AMZN) analysis in light of the results of the last quarter.

#1 Price vs. Growth

First of all, let's assess whether we can statistically state that Amazon's growth has accelerated or slowed down in the last quarter. To do this, let's compare the revenue growth trends of the key segments of the company with and without the results of the last four quarters.

The dynamics of the 'Online Stores' segment showed a qualitative breakthrough. Without taking into account the last four quarters, a near-linear trend was observed here. Now, it has become exponential:

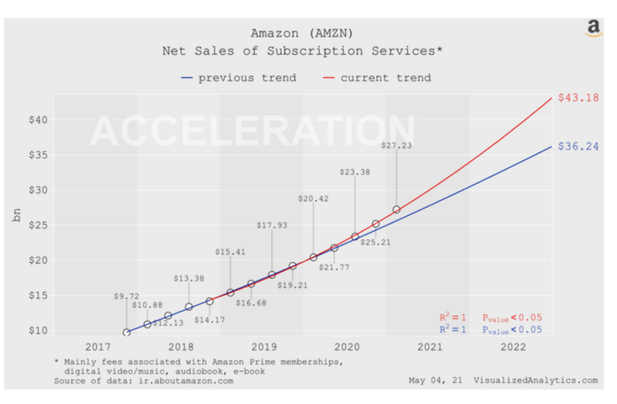


Source: VisualizedAnalytics.com

The 'Third-Party Seller Services' segment - the exponential growth continues:

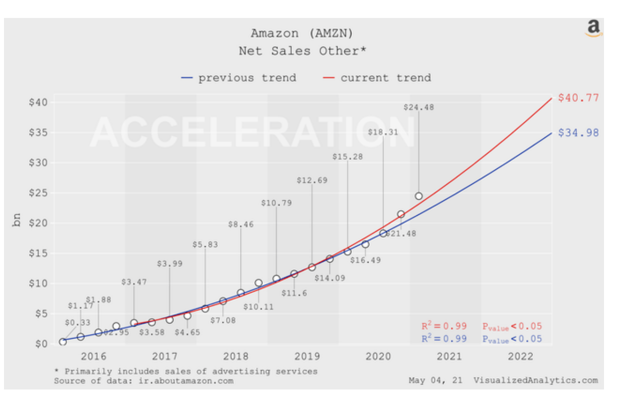
Source: VisualizedAnalytics.com

The 'Subscription Services' (Amazon Prime) segment - here the acceleration remains, and the result of the last quarter was better than the trend:



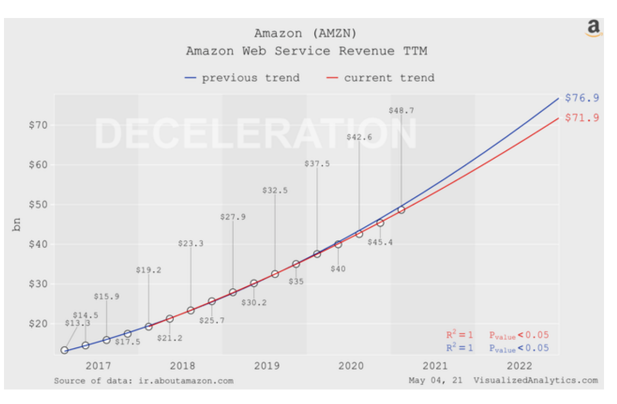
Source: VisualizedAnalytics.com

The 'Other' (advertising services) segment has also showed a significant acceleration:



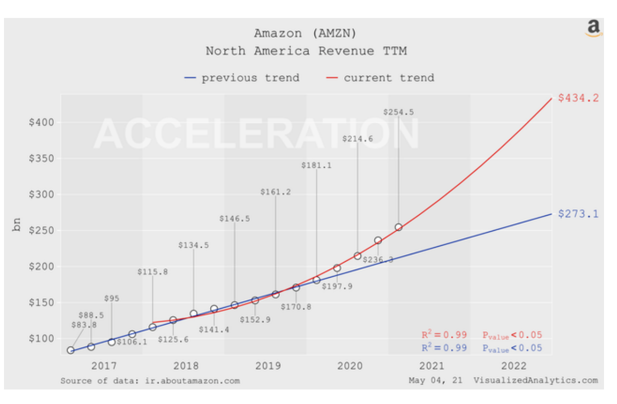
Source: VisualizedAnalytics.com

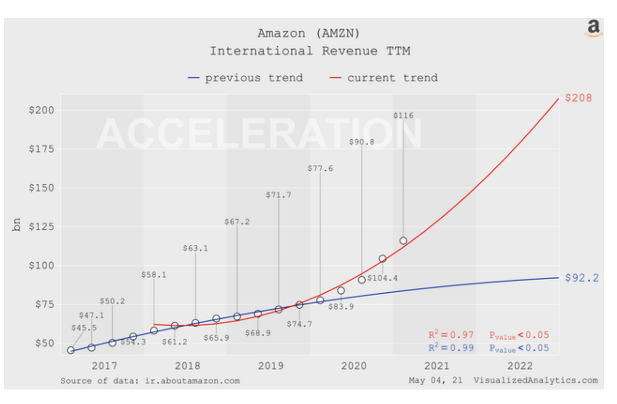
The growth trend of 'Amazon Web Services' has slowed down, but judging by the results of the last quarter, there is a gradual return to the previous trend:



Source: VisualizedAnalytics.com

Geographically, Amazon's revenue was also significantly better than the trend:

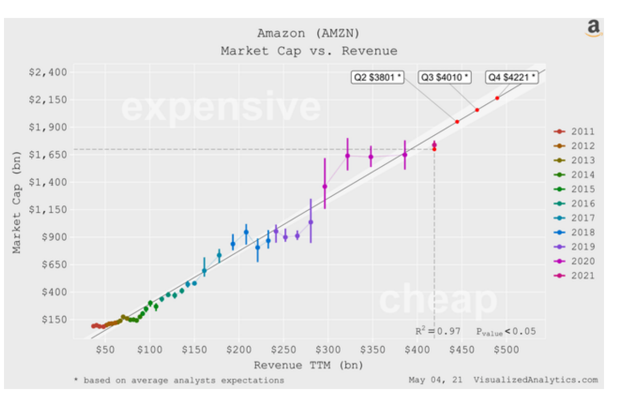




Source: VisualizedAnalytics.com

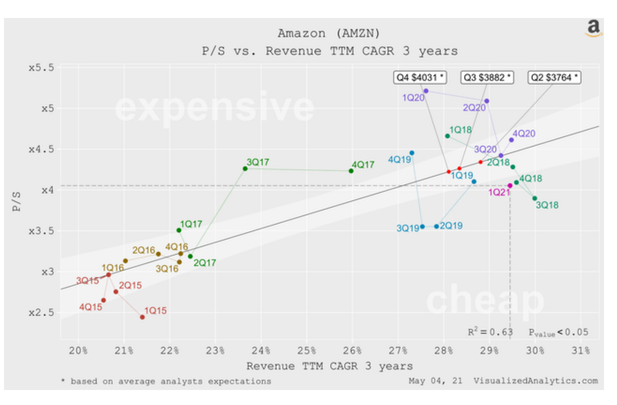
*So, statistically, not subjectively, we should recognize the acceleration of the company's growth **in all key segments**. In my opinion, this is exactly what is expected from Amazon.*

Further. Over the last 10 years, Amazon's capitalization has been in a qualitative linear relationship with its revenue:



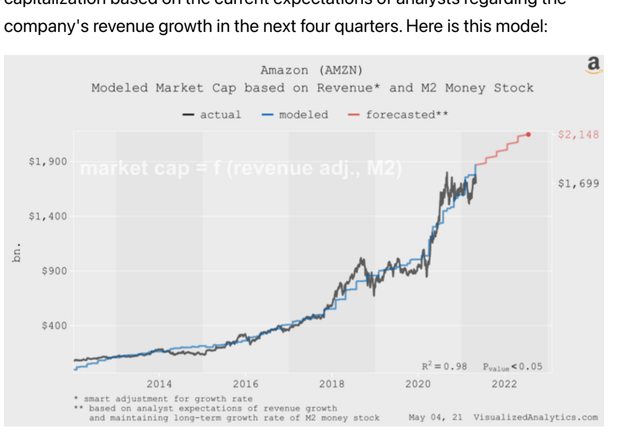
Source: VisualizedAnalytics.com

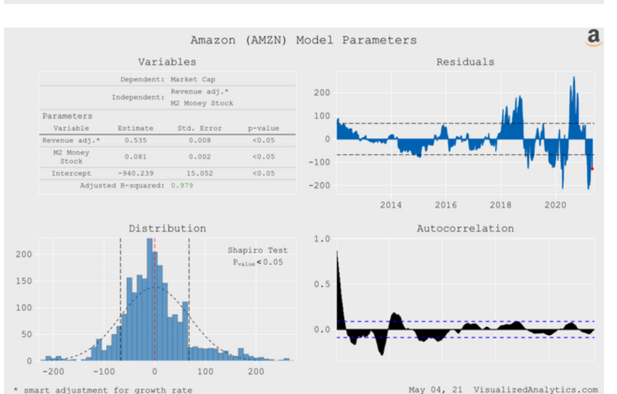
There is also a certain influence of the company's revenue growth rate on its multiples:



Source: VisualizedAnalytics.com

Based on these two relationships and taking into account the influence of the growth of the M2 money stock in the US, it is possible to build another model that allows us to determine the balanced level of the company's capitalization. In addition, this model allows to model the growth of the company's capitalization based on the current expectations of analysts regarding the company's revenue growth in the next four quarters. Here is this model:



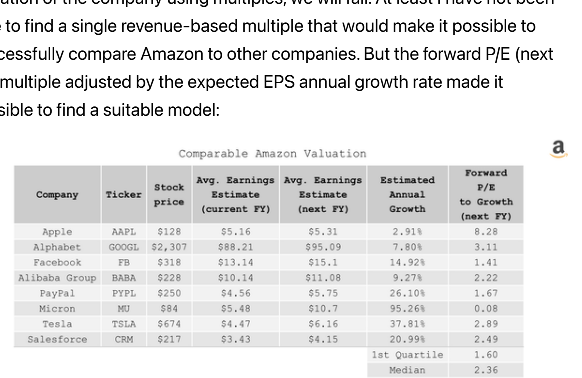


Source: VisualizedAnalytics.com

*As you can see, firstly, this model indicates that the company's current price is already **below the balanced level**. And secondly, it assumes a **25% growth** in capitalization in the next four quarters.*

#2 Comparative Valuation

In the previous block, I modeled Amazon's balanced price based on revenue. What is remarkable is that if we apply the same approach to the comparative valuation of the company using multiples, we will fail. At least I have not been able to find a single revenue-based multiple that would make it possible to successfully compare Amazon to other companies. But the forward P/E (next FY) multiple adjusted by the expected EPS annual growth rate made it possible to find a suitable model:



Comparable Amazon Valuation

Company	Ticker	Stock price	Avg. Earnings Estimate (current FY)	Avg. Earnings Estimate (next FY)	Estimated Annual Growth	Forward P/E to Growth (next FY)
Apple	AAPL	$128	$5.16	$5.31	2.91%	8.28
Alphabet	GOOGL	$2,307	$88.21	$95.09	7.80%	3.11
Facebook	FB	$318	$13.14	$15.1	14.92%	1.41
Alibaba Group	BABA	$228	$10.14	$11.08	9.27%	2.22
PayPal	PYPL	$250	$4.56	$5.75	26.10%	1.67
Micron	MU	$84	$5.48	$10.7	95.26%	0.08
Tesla	TSLA	$674	$4.47	$6.16	37.81%	2.89
Salesforce	CRM	$217	$3.43	$4.15	20.99%	2.49
					1st Quartile	1.60
					Median	2.36
					3rd Quartile	2.95
Amazon	AMZN	$3,312	$54.11	$70.93	31.08%	1.50
						Implied Share Price
					1st Quartile	$3,536
					Median	$5,194
					3rd Quartile	$6,497

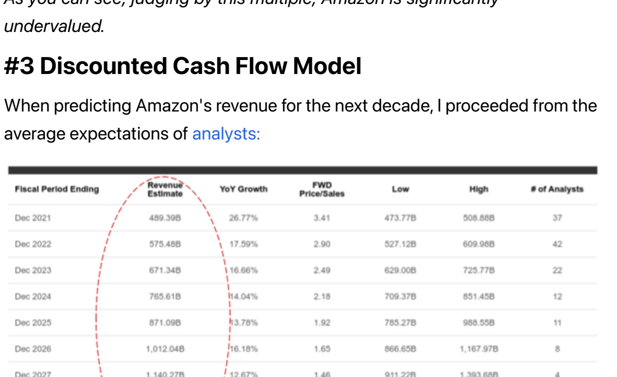
May 04, 21 VisualizedAnalytics.com

Source: VisualizedAnalytics.com

As you can see, judging by this multiple, Amazon is significantly undervalued.

#3 Discounted Cash Flow Model

When predicting Amazon's revenue for the next decade, I proceeded from the average expectations of analysts:

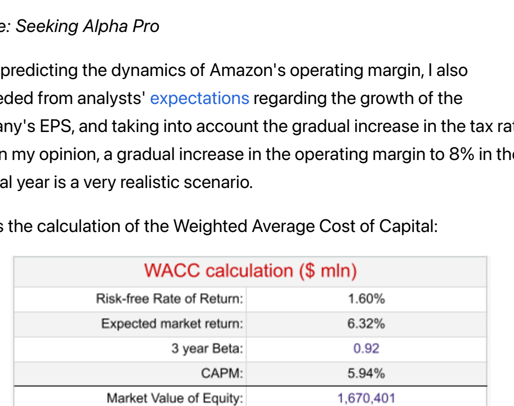


Fiscal Period Ending	Revenue Estimate	YoY Growth	FWD Price/Sales	Low	High	# of Analysts
Dec 2021	489.39B	26.77%	3.41	473.77B	508.88B	37
Dec 2022	575.48B	17.59%	2.90	527.12B	609.98B	42
Dec 2023	671.34B	16.66%	2.49	629.00B	725.77B	22
Dec 2024	765.61B	14.04%	2.18	709.37B	851.45B	12
Dec 2025	871.09B	13.79%	1.92	785.27B	988.55B	11
Dec 2026	1,012.04B	16.18%	1.65	866.65B	1,167.97B	8
Dec 2027	1,140.27B	12.67%	1.46	911.22B	1,393.68B	4
Dec 2028	1,278.81B	12.15%	1.31	958.45B	1,663.70B	4
Dec 2029	1,434.86B	12.20%	1.16	1,008.51B	1,986.88B	4
Dec 2030	1,610.91B	12.27%	1.04	1,061.81B	2,373.89B	4

Source: Seeking Alpha Pro

When predicting the dynamics of Amazon's operating margin, I also proceeded from analysts' expectations regarding the growth of the company's EPS, and taking into account the gradual increase in the tax rate to 25%. In my opinion, a gradual increase in the operating margin to 8% in the terminal year is a very realistic scenario.

Here is the calculation of the Weighted Average Cost of Capital:



WACC calculation ($ mln)	
Risk-free Rate of Return:	1.60%
Expected market return:	6.32%
3 year Beta:	0.92
CAPM:	5.94%
Market Value of Equity:	1,670,401
Market Value of Debt:	84,935
Total market value of equity & debt:	1,755,336
Equity:	95.16%
Debt:	4.84%
Tax Rate:	25%
After Tax Cost of Debt:	1.67%
Cost of Equity:	5.65%
WACC:	5.46%

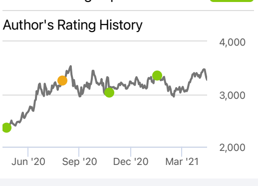
Source: Author

Some explanations:

- In order to calculate the market rate of return, I used values of equity risk premium (4.72%) and the current yield of UST10 as a risk-free rate (1.6%).
- I used the current value of the three-year beta coefficient (0.92). For the terminal year, I used Beta equal to 1.
- To calculate the Cost of Debt, I used the interest expense for 2019 and 2020 divided by the debt value for the same years.

Here is the model itself:

About This Article
Ticker Covered AMZN
Author's rating at publication Bullish
Author's Rating History



About AMZN

Symbol	Last Price	% Chg
AMZN	3,270.54	-1.25%
Post	3,269.99	-0.02%

1D 5D 1M 6M 1Y 5Y 10Y

PE (FWD)	61.44
Yield (FWD)	-
Rev Growth (YoY)	41.47%
Short Interest	1.28%

Compare to Peers

AMZN Ratings

SA Author	Neutral	3.48
Wall Street	Very Bullish	4.78
Quant	Neutral	3.37

Quant Ranking

Sector	Consumer Discretionary
Industry	Internet and Direct Marketing Retail
Ranked in Industry	4 out of 43
Ranked in Sector	127 out of 434
Ranked Overall	1069 out of 3945

Quant ratings beat the market »

More on AMZN
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Amazon: Still Another 40% Upside Potential From Here

SA Connect

Total Revenue:	88,989	107,007	135,987	177,866	232,887	280,522	386,064	489,390	575,480	671,260	764,050	867,070	1,004,890	1,110,490	1,250,460	1,408,750	1,558,270	1,583,202
Total Revenue Growth Rate:	19.52%	20.2%	27.1%	30.8%	30.9%	20.5%	37.6%	26.8%	17.6%	16.6%	13.8%	13.5%	15.9%	10.5%	12.6%	12.7%	10.6%	1.6%
Total Operating Income:	2,130	2,233	4,186	4,106	12,420	14,540	22,899	29,363	35,737	43,144	50,827	59,699	71,610	81,905	95,456	111,303	127,426	133,996
Operating Margin:	2.4%	2.1%	3.1%	2.3%	5.3%	5.2%	5.9%	6.0%	6.2%	6.4%	6.7%	6.9%	7.1%	7.4%	7.6%	7.9%	8.2%	8.5%
Tax Rate:	93.82%	42.5%	34.0%	18.7%	9.64%	16.3%	12.5%	15.0%	18.0%	20.0%	22.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Tax:	(1,998)	(950)	(1,425)	(769)	(1,197)	(2,374)	(2,863)	(4,405)	(6,433)	(8,629)	(11,182)	(14,925)	(17,902)	(20,476)	(23,864)	(27,826)	(31,856)	(33,499)
Net Operating Profit After Tax (NOPAT):	132	1,283	2,761	3,337	11,223	12,166	20,036	24,959	29,305	34,515	39,645	44,774	53,707	61,428	71,592	83,477	95,569	100,497
Adjustments for Non-Cash Charges:																		
Depreciation & Amortization:	4,746	6,281	8,116	11,478	15,341	21,789	25,251	31,125	36,600	42,692	48,593	55,145	63,910	70,627	79,529	89,596	99,105	112,840
% Revenue:	5.33%	5.87%	5.97%	6.45%	6.59%	7.8%	6.5%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	
Share-based compensation:	1,497	2,119	2,975	4,215	5,418	6,864	9,208	10,751	12,643	14,747	16,785	19,049	22,077	24,396	27,471	30,949	34,234	34,782
% Revenue:	1.7%	2.0%	2.2%	2.4%	2.3%	2.4%	2.4%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%
Deferred income taxes:	(316)	81	(246)	(29)	441	796	(554)	(103)	(121)	(141)	(160)	(182)	(211)	(233)	(263)	(296)	(327)	(332)
% Revenue:	-0.4%	0.1%	-0.2%	0.0%	0.2%	0.28%	-0.14%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%	-0.02%
Other:	182	286	(689)	(90)	493	(85)	(2,653)	(413)	(486)	(567)	(645)	(732)	(849)	(938)	(1,056)	(1,190)	(1,316)	(1,337)
% Revenue:	0.2%	0.3%	-0.5%	-0.1%	0.21%	-0.03%	-0.69%	-0.1%	-0.08%	-0.08%	-0.08%	-0.08%	-0.08%	-0.08%	-0.08%	-0.08%	-0.08%	-0.08%
Changes in Working Capital:																		
Accounts receivable:	(1,039)	(1,755)	(3,436)	(4,780)	(4,615)	(7,681)	(8,169)											
Inventories:	(1,193)	(2,187)	(1,426)	(3,583)	(1,314)	(3,278)	(2,849)											
Accounts payable:	1,759	4,294	5,030	7,100	3,263	8,193	17,480											
Accrued expenses and other:	706	913	1,724	283	472	(1,383)	5,754											
Unearned revenue:	4,433	7,401	1,955	738	1,151	1,711	1,265											
Amortization of previously unearned revenue :	(3,692)	(6,109)	(9,976)	-	-	-	-											
(Increase)/decrease in NWC:	974	2,557	(6,129)	(242)	(1,043)	(2,438)	13,481	(2,020)	(2,375)	(2,770)	(3,153)	(3,578)	(4,147)	(4,583)	(5,160)	(5,813)	(6,430)	(6,533)
% Revenue:	1.1%	2.4%	-4.5%	-0.1%	-0.4%	-0.9%	3.5%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%	-0.4%
CAPEX:	(4,893)	(5,387)	(7,804)	(11,955)	(13,427)	(16,861)	(40,140)	(31,577)	(37,503)	(44,182)	(50,793)	(58,218)	(68,146)	(76,060)	(86,504)	(98,428)	(109,964)	(112,840)
% Revenue:	-5.5%	-5.0%	-5.7%	-6.7%	-5.8%	-6.0%	-10.4%	-6.5%	-6.5%	-6.6%	-6.6%	-6.7%	-6.8%	-6.8%	-6.9%	-7.0%	-7.1%	-7.1%
Unlevered Free Cash Flow:								32,723	38,063	44,294	50,272	56,258	66,342	74,637	85,609	98,295	110,871	3,047,370
Discount Rate (WACC):								5.46%	5.46%	5.46%	5.46%	5.46%	5.46%	5.46%	5.46%	5.46%	5.46%	5.77%
PV of FCF:								31,028	34,222	37,762	40,639	43,122	48,218	51,437	55,943	60,906	65,140	1,739,002
PV of CF:	2,207,420																	
Debt:	(84,935)																	
Cash + Marketable securities:	73,270																	
Implied Equity Value:	2,195,755																	
Outstanding Shares:	513																	
Current Market Capitalization:	1,699,138																	
Current price:	3,312																	
Fair value per share:	4,280.2																	
Potential:	29.2%																	

@oleh_kombaiev for Seeking Alpha

(In high resolution)

Source: Author

The DCF-based target price of Amazon's shares is $4,280, offering 29% upside.

Final thoughts

1. Amazon is one of the companies whose growth has not yet reached its limit and not even entered the plateau phase. In a sense, this is a startup with $73 billion cash.
2. The fact that Amazon remains in the acceleration phase does not mean that its capitalization is constantly undervalued. But in this case, based on the patterns between the company's capitalization and the parameters of its revenue, we can conclude that the company is **undervalued**.
3. Comparing Amazon to other companies through the prism of expected EPS growth, it must be admitted that the company is **much cheaper** than the market.
4. DCF model based on average expectations analysts indicate a 30% undervaluation. At the start of the year, a similar model indicated a 20% undervaluation.
5. When you look at Amazon's revenue forecast for the next decade, you realize that the company will face growth problems. But in my opinion, *it is better to invest in a company facing growth problems than aging problems*.

This article was written by

Oleh Kombaiev Following
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Disclosure: I/we have no positions in any stocks mentioned, and no plans to initiate any positions within the next 72 hours. I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.

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Comments (570)

Thanks for this excellent article!

Long AMZN since 2 years....

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Amazon is a beast....price target 6666 ..... thats the number!

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Thank you for the article

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Oleh, wonderful article and I've finally come around to Amazon after many years of sitting it out. Jeff Bezos is a brilliant capital allocator.

I would love an article on FB and it's media properties including Instagram and WhatsApp. Would like your thoughts on how Apple's new privacy policies will impact FB's advertising revenue. Google will be less impacted as they have search.

Would also like your view of WhatsApp and it's payment model, they've re-introduced this into Brazil. FB controls social connections globally, if they can control digital money flows (P2P then B2C) it could be a misunderstood game changer for the stock.

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Marketplace Comments (55) | + Follow

Thorough & accurate, well written 💯

Reply Like (1)

sg14789 Today, 12:15 AM
Premium Marketplace Comments (18) | + Follow

There is no doubt that AMZN is underpriced but the share price is too high for the average investor. Until there is a stock split to make the price of the company more attractive to the masses this stock will be range bound. *(edited)*

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@sg14789 fractional shares?

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sg14789 Today, 1:50 AM
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@Munderah St yes you can trade fractional shares, but it is kind of like owning a timeshare. You only own a small part of one share. Doesn't feel the same as owning a full share.

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MikeFromNZ Today, 12:12 AM
Marketplace Comments (1.56K) | + Follow

It's interesting that both AMZN and its Chinese counterpart BABA are undervalued by these metrics.

I wonder what "the market" systematically doesn't like or doesn't appreciate about these businesses?

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